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Supreme

Realty Associates

Edwin B. [illegible], James H. [illegible] and
Zaidenberg, as Members of the [illegible]
tive Committee,

Petitioners,

vs.

Realty Associates Securities Corporation and
Consolidated Realty Corporation,

Respondents.

PETITION OF BONDHOLDERS' PROTECTIVE COMMITTEE FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

David Saxe Rifkin, and
Bernard D. Cahn,
Counsel for Petitioners.

Julius Silver, and
Lewis, Marks & Kantor,
Attorneys for Bondholders' Protective Committee.

October 18, 1947.

The Court Press, N. Y. C.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1947.

No. .

In the Matter

of

REALTY ASSOCIATES SECURITIES CORPORATION,

Debtor.

EDWIN B. MEREDITH, JACOB R. SCHIFF and MILTON C. ZAIDENBERG, as Members of the Bondholders' Protective Committee,

Petitioners,

vs.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,

Respondents.

PETITION OF BONDHOLDERS' PROTECTIVE COMMITTEE FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Edwin B. Meredith, Jacob R. Schiff and Milton C. Zaidenberg, members of the Bondholders' Protective Committee, who have represented Bondholders throughout these proceedings, pray that a writ of certiorari be issued to review the judgment of the United States Circuit Court of Appeals for the Second

Circuit, entered July 23, 1947, modifying so much of an order of the United States District Court for the Eastern District of New York, dated August 5, 1946, as provided: (1) that the Bondholders of the Debtor should be paid interest on their claims at the rate of 6% per annum, from October 1, 1943, the date of maturity of the Bonds, to April 15, 1945, the date of payment fixed by the District Court in its order dismissing the proceeding for the reorganization of the Debtor under Chapter X of the Bankruptcy Act; and (2) that the claims upon which said interest should be paid included not only the matured principal amount of the Bonds, but also all interest accrued thereon to the maturity date.

Opinions.

The opinion of the District Court (R. 171) is reported at 66 F. Supp. 416. The opinion of the Circuit Court of Appeals (R. 209) is not yet reported.

Jurisdiction.

The judgment of the Circuit Court of Appeals was filed July 23, 1947 (R. 222). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended.

Questions Presented.

(1) Whether, in a voluntary reorganization proceeding under Chapter X of the Bankruptcy Act, instituted by a solvent debtor, the public bondholders shall receive less favorable treatment, in respect of interest accruing on their claims during the proceed-

ing, than they would receive in an ordinary bankruptcy case.

(2) Whether, during a voluntary reorganization proceeding under Chapter X of the Bankruptcy Act, instituted by a solvent debtor, interest accrues on the entire claim of the public bondholders, including in such claim the interest accrued, as well as the principal due, at the maturity date of the bonds.

(3) Whether, in such a proceeding, interest shall be paid to the debtor's public bondholders on their matured claims at the legal or judgment rate, or at a lesser rate referred to in the indenture under which the bonds are outstanding.

Statute Involved.

The pertinent provisions of the Bankruptcy Act (11 U. S. C., par. 1, *et seq.*) are set forth herein where appropriate.

Statement.

The facts in this case are not in dispute.

The Debtor, Realty Associates Securities Corporation, is incorporated and has its principal place of business in New York. It is engaged in the business of dealing in mortgages and other real estate securities and interests (R. 4-5). Its sole stockholder is Consolidated Realty Corporation (R. 7).

The principal indebtedness of the Debtor on September 28, 1943, the date of the filing of its voluntary petition for reorganization under Chapter X, was a publicly-held bond issue of which the principal amount then outstanding was $5,710,400. The bond issue

matured, without acceleration, on October 1, 1943, three days after the petition was filed (R. 6).*

The Bonds here involved were originally distributed to the public in 1925, 1927 and 1928, when the Debtor sold three bond issues of $5,000,000 principal amount each, maturing, respectively, in 1937, 1939 and 1943 (R. 5, 8). The Bonds were coupon bonds and originally bore the Debtor's unconditional obligation to pay interest at the rate of 6% per annum (R. 42, 52, 62). The Debtor filed a voluntary petition in bankruptcy on July 10, 1933, at which time an aggregate of $12,450,000 principal amount of such Bonds was outstanding (R. 5, 8). In April, 1934, the Debtor effected a composition, whereunder it made a cash payment of 15% on account of the indebtedness (including interest accrued to the date of the petition), reducing its debt to $10,598,575 (R. 5).

The adjusted principal amount was subject to a new Indenture, dated as of July 10, 1933 (R. 71), under which the maturity date of the modified bond issue was fixed as October 1, 1943 (R. 78). Interest on the adjusted Bonds was placed on an "if earned" basis, and the interest rate was reduced from 6% to 5% per annum (R. 79). Under the new Indenture, the Debtor was permitted to deduct capital losses from "earnings", for interest purposes, with the proviso, however, that such capital losses should not be deducted so as to reduce the interest to less than 3% per annum (R. 10, 94-95). Unpaid portions of

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* No point has been made by any of the parties hereto, based upon the period of three days intervening between the filing of the petition and the maturity date of the Bonds. For all practical purposes, such period will be deemed inconsequential, and the two dates will be considered as one.

the 5% annual interest obligation were made cumulative and payable out of future earnings, or at maturity (R. 10, 92-93). The 6% coupons were detached from the Bonds, which were stamped to indicate the modifications effected (R. 77).

Interest payments made after the composition and prior to the maturity of the modified Bonds approximated 3% per annum so that as of October 1, 1943, the date of maturity, there was an accumulation of unpaid interest in the amount of $1,286,646.43 (R. 147, 191). Deferment of such interest during the period from 1934 to 1943 was permitted by the unusual definition of earnings contained in the new Indenture.* During the same period, however, the Debtor repurchased $4,888,175 principal amount of the Bonds (R. 16) and, as of October 1, 1943, the principal amount outstanding was $5,710,400 (R. 6, 191).

The Debtor's petition for reorganization, dated September 28, 1943, alleged the Debtor's inability to meet its maturing indebtedness, but stated that the value of the Debtor's assets exceeded its total liabilities, including its capital stock. Debtor further alleged that its assets consisted largely of real estate and real estate securities, and that resort was made to Chapter X for a plan of reorganization which would "protect the bondholders and other creditors * * * and * * * reduce the loss to its stockholders which would otherwise result from the enforcement of bondholders' claims * * *" (R. 6).

The strenuous opposition of the Debtor to the at-

* See R. 138 for computation of earnings under the Indenture, which permitted a restricted deduction of "capital losses" and consequent reduction of interest payment, even though the Debtor's earnings were sufficient for additional interest payments.

tempts of Bondholders to protect their interests gave rise to considerable litigation in the course of the reorganization proceeding. At the instance of Bondholders, Jerome Thralls, the designee of Reconstruction Finance Corporation (which owned the stock of Debtor's sole stockholder) was removed as additional trustee (144 F. (2d) 473; cert. den. 323 U. S. 758, 89 L. Ed. 607). A Bondholders' committee friendly to the Debtor was disqualified (56 F. Supp. 1008). The Bondholders' list was freed from impoundment over the Debtor's opposition (144 F. (2d) 594), and prompt distribution to the Bondholders of large amounts of available cash was directed (58 F. Sup. 220). On April 2, 1945, the reorganization proceeding was dismissed upon motion of the Debtor and its sole stockholder, Consolidated Realty Corporation (R. 7, 25), when the latter finally advanced the funds necessary to pay the Bondholders (R. 13, 26). In their petition for dismissal, however, the Debtor and its stockholder put in issue their liability for interest beyond 5% on the unpaid principal to April 15, 1945, the date fixed for payment and settlement (R. 11, 14, 172).

The District Court's order dismissing the proceeding provided for payment of the undisputed claims for principal and interest (including interest accrued on principal during the proceeding, which was not disputed by the Debtor) and for a reserve to be retained by the Reorganization Trustees appointed under Chapter X, sufficient for payment of any additional amounts which might be allowed (R. 25-41). In dismissing the Chapter X proceeding, the District Court reserved jurisdiction to adjudicate, *inter alia*, the dispute as to the proper interest rate and the proper base upon which such interest should be paid (R. 38), the Bondholders con-

tending that interest at the rate of 6% should be allowed upon the entire claim (including in the claim interest accrued to the maturity date of the Bonds), while the Debtor contended that interest at the rate of 5% for the period of the proceeding should be paid only on the matured principal amount of the Bonds (R. 11, 14, 170).

The District Court decided that interest should be allowed at the rate of 6% on the Bondholders' entire claim, including unpaid principal and interest accrued to the date of maturity (R. 171-181, 191). The Circuit Court of Appeals reversed (Clark, *J.*, dissenting), holding, in effect, that interest at the rate of 5%, the rate referred to in the Indenture dated July 10, 1933, should be paid for the period of the proceeding and that interest at the 5% rate was payable only on that portion of the claim which represented the matured principal of the Bonds (R. 209, *et seq.*).

Specification of Errors to Be Urged.

The court below erred:

(1) in failing to allow interest on the entire claim of the Bondholders, as filed and allowed in the proceeding, including that portion of the claim representing interest accrued and unpaid at the maturity date of the Bonds;

(2) in refusing to hold that the claim of the Bondholders, as filed and allowed in the proceeding, had the efficacy of a judgment for purposes of administration under the Bankruptcy Act, and that upon such claim the legal or judgment rate of 6% was payable;

(3) in holding that the Bondholders were entitled to receive less, in respect of interest on their claims

as filed and allowed in the proceeding, than they would have received in an ordinary bankruptcy proceeding;

(4) in predicating its holdings on an interpretation of the Indenture dated July 10, 1933, and on the local law applicable thereto, rather than upon equitable considerations applicable to such matters in proceedings under the Federal Bankruptcy Act;

(5) in interpreting the said Indenture to require the payment of 5% rather than 6% interest after maturity.

Reasons for Granting the Writ.

The majority decision of the Circuit Court of Appeals below is contrary to decisions in analogous cases in this Court and in other Circuit Courts of Appeal. While the precise question here involved is one of first impression in reorganization cases under Chapter X of the Bankruptcy Act, the decisions of this Court and of Circuit Courts of Appeal, in cases arising under the ordinary bankruptcy provisions of the Act and in other analogous cases, are contrary to the holding of the Circuit Court in the instant case. As a result, the lower court's decision here will create confusion in the administration of the Bankruptcy Act and will result in less favorable treatment of creditors in Chapter X proceedings than they would receive in ordinary bankruptcy proceedings, contrary to the intention of the statute.*

The Debtor does not question that under proper equitable principles the Bondholders were entitled to interest accrued during the proceeding. The dispute here is as to the base and rate of payment. Peti-

* See Sections 102 and 200 of the Bankruptcy Act (11 U. S. C., par. 502, 600).

tioners herein contend that the Bondholders are entitled to interest based on the full amount of their allowed claims, including in such base the interest accrued at the maturity rate of their Bonds; and that interest should accrue on such claim at the legal or judgment rate of 6%. The payment of any lesser amount of interest to the Bondholders will result in a windfall to the Debtor's sole stockholder.

The contest here is between the Debtor (and its sole stockholder) and the Debtor's public Bondholders. There are no other public security holders. The reorganization petition was voluntarily filed by a solvent Debtor whose resources proved ample to make substantial payments to the Bondholders during the proceeding. The delay made possible by the proceeding during a period of rising real estate values enabled the Debtor to readjust its affairs and obtain a dismissal of the proceeding. On every important point, therefore, the facts here differ significantly from the factual situation which existed in the *Vanston* case,* where this Court decided that the equities in favor of public junior security holders rendered it inappropriate to pay full accrued interest to the senior bondholders. Further, in contradistinction to the *Vanston* case, the interest which forms part of the Bondholders' claim here, and on which interest is now sought, had accrued at the time of the filing of the Debtor's petition and not during the course of the proceeding.

Base for Interest Computation.

The holding of the Circuit Court of Appeals below that interest should be paid to the Bondholders only on that portion of their claims which represented

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* *Vanston Bondholders' Protective Committee* v. *Green, et al.*, 67 Sup. Ct. 237; 91 L. Ed. (Advance Opinions) 175 (1946).

matured principal, and not on the claim for interest accrued as of the maturity date of the Bonds, is contrary to the governing provisions of the Bankruptcy Act, and to analogous prior decisions.

Section 63(a)(1) of the Bankruptcy Act (11 U. S. C., par. 103(a)(1)) provides:

> "Debts of the bankrupt may be proved and allowed against his estate which are founded upon (1) a fixed liability as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition by or against him, whether then payable or not, *with any interest thereon which would have been recoverable at that date* * * *." (Emphasis added.)

Under a provision in the Bankruptcy Act of 1867, similar to Section 63, it was held that before any surplus could be turned over to a solvent bankrupt, interest should be paid from the date of adjudication (the date when claims were provable under the 1867 Act) to the date of payment, upon proven claims consisting of principal plus interest accrued thereon to the date of adjudication.

> *In re Town*, Fed. Cas. No. 14, 112, 24 Fed. Cas. 85 (E. D. Mich. 1873);
> *In re Hagan*, Fed. Case No. 5898, 11 Fed. Cas. 154 (S. D. N. Y., 1873).

See also:

> *In re Bank of North Carolina*, Fed. Case No. 895, 2 Fed. Cas. 667 (W. D. N. C., 1875).

In *Johnson* v. *Norris,* 190 Fed. 459 (C. C. A. 5, 1911), decided under the 1898 Bankruptcy Act, the court required the Trustee to pay interest on all approved claims from and after the date of the filing of the petition; and it appears from the case that such claims included interest to the date of the filing of the petition.

In *Ryerson and Son* v. *Peden,* 318 Ill. 105, 148 N. E. 849 (1925), which involved a claim in bankruptcy, the Illinois Supreme Court held that allowed claims which included fixed liabilities, plus interest accrued to the date of the bankruptcy petition, had the efficacy of judgments for the purpose of determining the base for the accrual of interest after the filing of the petition.

Similar principles have been applied in equity receiverships. In *Ohio Savings Bank and Trust Co.* v. *Willys Corp.,* 8 F. (2d) 463 (C. C. A. 2, 1925), the allowed claims were fixed as of April 1, 1922 (the last date for the filing of claims), and included interest accrued to that date. Interest was allowed by the court for the period subsequent to April 1, 1922, on the total amount of the claims as above computed.

Hence, under the decisions, in bankruptcy and equity receivership proceedings, allowable claims include not only matured principal but also interest thereon accrued to the date of allowance of the claims. And, in such proceedings, where the debtors are solvent, creditors are entitled to receive interest on the full amount of such allowed claims.

The term "claims", for purposes of Chapter X, is even broader than that applicable to ordinary bank-

ruptcy proceedings. Section 106 of the Act* defines the term "claims", for purposes of Chapter X, as including "all claims of whatever character against a debtor or its property, except stock, whether or not such claims are provable under Section 63 of this Act and whether secured or unsecured, liquidated or unliquidated, fixed or contingent". Furthermore, the Act explicitly negatives the idea that creditors are to be treated less favorably in Chapter X than in ordinary bankruptcy proceedings. Section 200 of the Act (11 U. S. C., par. 600) provides:

> "Where not inconsistent with the provisions of this chapter, the rights, duties, and liabilities of creditors and of all other persons with respect to the property of the debtor shall be the same, before the approval of the petition, as in a bankruptcy proceeding before adjudication and, upon the approval of the petition, as in a bankruptcy proceeding upon adjudication."

No inconsistency in this case, within the meaning of the Act, precludes the application of the section. The claims of the Bondholders, as allowed by the Bankruptcy Court in the instant case, were indivisible and included interest accrued to the maturity date of the Bonds. Had this proceeding been an ordinary bankruptcy case, the Bondholders would have received interest on the full amount of their claims. The decision of the court below results in less favorable treatment of creditors in Chapter X cases, involving solvent debtors, than such creditors would receive in ordinary bankruptcy proceedings. Such a result is clearly erroneous.

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* 11 U. S. C., par. 506.

Interest Rate.

(1) The lower court was likewise in error in reducing the rate of interest allowable on the Bondholders' claims from 6% to 5%. Its decision on this point was contrary to principles established by this Court and by other Courts of Appeal.

This Court held in the *Vanston* case that the allowance by Federal courts of interest on claims against debtors' estates depends upon equitable considerations under Federal law. The touchstone of each decision in such cases is "a balance of equities between creditor and creditor or between creditors and the debtor" (91 L. Ed. Advance Opinions 179). In the instant case, the proper balance of equities between public Bondholders and the Debtor requires the payment to the Bondholders of full interest at the judgment rate.

The filing by the Debtor of its petition for reorganization was, in effect, a confession of judgment and a plea for relief against the alleged inequity to the Debtor of a forced sale of its assets. Under Chapter X, the filing of the petition prevented the Bondholders from reducing their undisputed claims to judgment. This restraint by the Bankruptcy Act was designed to prevent piecemeal disintegration of the Debtor's estate during the proceeding, and to preserve the Bankruptcy Court's control over the Debtor's entire estate, in order to assure fair and equitable treatment to all creditors. The statutory preclusion of the normal procedural remedies of Bondholders should not, however, deprive them of the substantive rights which would have attached to the entry of judgments on their Bonds. It is the intention of the statute that those substantive rights shall continue and shall be

fully recognized, with appropriate compensation for any change in position occasioned by the proceeding.

Cf. *Consolidated Rock Products Company* v. *DuBois,* 312 U. S. 510.

Where a creditor has been prevented by the filing of a reorganization petition from merging his claim for unpaid principal and interest into a single judgment debt which would bear interest at the judgment rate, he is equitably entitled to be accorded the same substantive rights as he would have possessed had the restraints of Chapter X not been imposed. His claim, when allowed, should have the same efficacy as a judgment and should occupy the same legal ground. Hence, the Bondholders' claims in the instant case are equitably entitled to be treated as judgments, and interest should be payable thereon at the rate of 6%.*

(2) The Bondholders' contention is not only grounded on general equitable principles, but is also supported by authoritative decisions in bankruptcy, receivership and liquidation cases. Such cases have consistently granted to creditors' claims the status of judgments, with full interest at the judgment rate allowable thereon, where the debtors in question were solvent or occupied comparable positions.

One of the earliest cases on the point is *National Bank of the Commonwealth of New York* v. *Mechanics National Bank,* 94 U. S. 437; 24 L. Ed. 176 (1877),

* 28 U. S. C. A., par. 811, provides that interest allowable on civil judgments shall be at the rate allowed by the laws of the state in which the Court is held. Judgments in New York bear the 6% legal rate of interest. See 19 McKinney's Consolidated Laws of New York Ann. (Gen. Bus. Law), Art. 25, par. 370.

which involved the liquidation of a bank under the National Banking Act. This Court there held that depositors were entitled to interest on demand deposits from the date of demand, at the rate applicable to judgments, stating (94 U. S. at 438-9):

> "The 50th section of the National Banking Act, 13 Stat. at L. 113, requires the Comptroller of the Currency to apply the moneys paid over to him by the receiver 'on all such claims as may have been proved to his satisfaction, or adjudicated in a court of competent jurisdiction'. The Act is silent as to interest upon the claims before or after proof or judgment. Can it be doubted that a judgment, if taken, would include interest down to the time of its rendition? Section 996 of the Revised Statutes, p. 182, declares that all judgments in the courts of the United States shall bear the same rate of interest as judgments in the courts of the States, respectively where they are rendered. Interest is allowed by the law of New York upon judgments from the time they are perfected. Rev. Code of N. Y. ed. 1859, Vol. III, p. 637.
>
> "If these claims had been put in judgment, whether in a court of the United States or in a state court of that state, the result as to interest upon the judgment would have been the same. It was unnecessary to reduce them to judgment, because they were proved to the satisfaction of the comptroller. After they were so proved, they were of the same efficacy as judgments, and occupied the same legal ground. Hence they are within the *equity* if not the letter of these statutes, and bear interest as judgments would have done * * *." (Emphasis supplied.)

Recent cases under the National Banking Act in which the same doctrine was involved include:

Stein v. *Delano,* 35 F. Supp. 260, aff'd. 121 F. (2d) 975 (C. C. A. 3, 1941), cert. den. 314 U. S. 655 (1941);

Elliott v. *First Inland National Bank of Pendleton,* 32 F. Supp. 839 (D. Ore., 1940).

The same principle was applied by the Second Circuit Court of Appeals in a bankruptcy case: *In re John Osborn's Sons & Co.,* 177 Fed. 184 (1910). In that case, the court, following the reasoning in *National Bank of the Commonwealth of New York* v. *Mechanics National Bank, supra,* concluded that "allowed claims in bankruptcy are entitled to be treated as judgments". See also *Ryerson and Son* v. *Peden,* 318 Ill. 105, 148 N. E. 849 (1925).*

The majority opinion of the Circuit Court in the instant case recognized that the doctrine in ordinary bankruptcy cases is that allowed claims are of the same efficacy as judgments. Nevertheless, the Court held that the principle is inapplicable to a Chapter X proceeding** "where the very purpose of the proceeding is to keep the debts in *statu quo* until a plan can be adopted under which the Debtor may continue in

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* While the policy of the New York courts is not controlling in these proceedings, it is relevant to note that such policy is the same. In the administration of debtors' estates, holders of matured claims are treated as judgment creditors.

Dorland v. *Fidelity Development Co.,* 104 Misc. 97, 99, 171 N. Y. Supp. 1000, 1001.

** The statutory intent, as expressed in Sections 102 and 200 of the Bankruptcy Act which apply to Chapter X proceedings the ordinary bankruptcy provisions of the Act, is contrary to the Circuit Court's conclusion.

business without having its property burdened with judgments" (R. 214). No provision of the Act or other appropriate authority is cited by the Circuit Court for that distinction, and we have been unable to find any.*

The majority opinion confuses the statutory mechanics of reorganization with the substantive rights of creditors. The mechanics of stay are essential to an orderly and effective proceeding, but the fact that creditors are stayed in the prosecution of their normal legal remedies is no basis for depriving them of a portion of the claim which they would have had but for the statutory restraints. The Circuit Court's holding is, in fact, contrary to the principle of full compensatory treatment to creditors for the sacrifices which they are required to make in Chapter X reorganization proceedings.

Consolidated Rock Products Company v. *DuBois, supra.*

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* The majority of the Court below were apparently influenced in their decision by their interpretation of the provisions of the Trust Indenture relating to the payment of interest under the laws of the State of New York. The conclusion based upon such considerations was clearly erroneous. As this Court held in the *Vanston* case [91 L. Ed. Advance Opinions 175, 178], Federal equitable principles and not local law should have governed the decision. Furthermore, it may be observed from a reading of the Circuit Court's opinion that the Trust Indenture was ambiguous in the matter of payment of interest after maturity. Under well-accepted principles of construction, such ambiguity should have been resolved in favor of the Bondholders rather than in favor of the Debtor.

Cunningham v. *Pressed Steel Car Company*, 238 App. Div. 624; aff'd. 263 N. Y. 671;
Enoch v. *Brandon*, 249 N. Y. 263, 268;
Barnes v. *United Steel Works Corpn.*, 11 N. Y. S. 2nd 161, 163.

The error in the majority's position is clearly and succinctly analyzed as follows in the dissenting opinion of Judge Clark below (R. 218-219):

> "* * * As the opinion [of the majority] substantially concedes, allowance of a claim in bankruptcy fixes it, just as does a judgment, and an ordinary judgment bears interest at the legal rate. The situation is one therefore where a debtor who has availed himself of the bankruptcy provisions ultimately is able to pay in full; he should not then be permitted to make use of the statute to reduce his claim. Obviously here, except for the proceedings, the creditors would have taken judgment at once; they should not be deprived of that advantage by the debtor's unassented-to act.
>
> "That this was a reorganization, rather than an ordinary bankruptcy, proceeding would seem not to change this situation. It is still only a question between the debtor and its creditors."

Summary and Conclusion.

The problem here is one of adjustment of equities between a solvent Debtor and its public Bondholders. The interest contended for by the Bondholders arose on a claim which was liquidated and matured at the commencement of the proceedings and included a debt for interest previously accrued. That interest accrued prior to the proceeding by reason of a definition of earnings in the Indenture which permitted the Debtor to defer payment of interest, although it had funds available for the purchase of its Bonds from the Bondholders.

On the eve of the maturity date of the principal and interest then accrued, the Debtor instituted its

second voluntary reorganization proceeding and obtained an 18-month respite, during which real estate and real estate securities appreciated substantially in value. During that period the Bondholders' funds were available to the Debtor for use in its business. Delay in payment enabled the Debtor to profit greatly by its leverage position in a rising market. Under these circumstances, it would be a gross inequity to deny to Bondholders any portion of their claims, including the interest to which they would have been entitled had the Debtor not resorted to proceedings in Chapter X.

The principles established by this Court require that creditors be paid in full for their enforced sacrifices. Not the least of the creditors' sacrifices here was their inability to realize upon their claims when due, and the consequent deprivation to them of the opportunity to benefit in a rising market. The equities clearly favor the Bondholders' contention that they should receive full payment of their claims.

Because the decision of the court below is contrary to well-established principles of bankruptcy law, and to the provisions of the Bankruptcy Act itself, and erroneously decides a question of public importance in the administration of the Act, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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October 18, 1947.

FILE COPY

Supreme Court of the

October Term,

No. 405

In the Matter

of

REALTY ASSOCIATES SECURITIES CORPORATION,

Debtor,

MANUFACTURERS TRUST COMPANY, Indenture Trustee,

Petitioner,

vs.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,

Respondents.

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Supreme Court of the United States

OCTOBER TERM, 1947.

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Respondents.

Stipulation.

IT IS HEREBY STIPULATED, CONSENTED AND AGREED that any Exhibits handed up upon the argument before the Circuit Court of Appeals, Second Circuit, pursuant to the Stipulations appearing at pages 200, 203 and 205 of the Transcript of Record used in that Court, may be included as appendices to any brief presented to the Supreme Court of the United States upon the application for writ of certiorari to review the judgment of said Circuit Court dated July 23, 1947, and in event

writ is granted, may be included in the transcript of record on appeal to the Supreme Court.

Dated: New York, N. Y., September 26th, 1947.

NEWMAN & BISCO,
Newman & Bisco, Attorneys for
Manufacturers Trust Company.

GEORGE ZOLOTAR,
George Zolotar, Attorney for
Securities & Exchange
Commission.

ROOT, BALLANTINE, HARLAN, BUSHBY
& PALMER,
Root, Ballantine, Harlan, Bushby
& Palmer, Attorneys for Con-
solidated Realty Corporation.

HOOKER, ALLEY & DUNCAN,
Hooker, Alley & Duncan,
Attorneys for the Debtor.

United States Circuit Court of Appeals
FOR THE SECOND CIRCUIT.

In the Matter
of
REALTY ASSOCIATES SECURITIES CORPORATION,
Debtor.

In the Matter of the Determination of the Amount of Interest Payable in Respect of the Debtor's Bonds After Maturity.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,
Appellants.

Complete Petition of Debtor Under Chapter X, Without Attached Exhibits (Only Part of Which Appears in Record, Fols. 12-20), Referred to in Brief of Appellees Manufacturers Trust Company, the Indenture Trustee, and Parties in the Armed Services.

HANDED UP AT THE ARGUMENT, PURSUANT TO STIPULATION (fol. 614).

PETITION OF DEBTOR UNDER BANKRUPTCY ACT, CHAPTER X.

[Without attached exhibits.]

(No. 45024)

(In Proceedings for the Reorganization of a Corporation.)

To the Honorable Judges of the District Court of the United States for the Eastern District of New York:

The petition of Realty Associates Securities Corporation respectfully represents:

1. Your petitioner is a corporation organized and existing under the laws of the State of New York and is a corporation which could become a bankrupt under the Act of Congress Relating to Bankruptcy, and is not a municipal, insurance or banking corporation or a building and loan association, or a railroad corporation authorized to file a petition under Section 77 of said Act.

Your petitioner now has and for more than ten years next preceding the filing of this petition has had its principal office and place of business at No. 162 Remsen Street, in the Borough of Brooklyn, County of Kings and State of New York, within the territorial jurisdiction of this Court.

2. The nature of the business of your petitioner is to buy, sell, administer and deal generally in mortgages and real estate securities and real property acquired by reason thereof and in interests or estates therein, and to make mortgage loans to and enter into contracts and agreements with builders, property owners, and others.

3. That on July 10, 1933, your petitioner filed a voluntary petition in bankruptcy in this Court, and thereafter offered terms of composition dated October 26, 1933, to its creditors, affecting particularly its three bond issues of 1925, 1927 and 1928, each originally in principal amount of $5,000,000 and maturing respectively July 1, 1937, December 1, 1939 and October 1, 1943; that said terms of composition were accepted by the creditors of your petitioner, and pursuant thereto, an Indenture, dated as of the 10th day

of July, 1933, was made between your petitioner and Manufacturers Trust Company, as Trustee, under which the bonded debt of your petitioner then in principal amount $12,450,000 was reduced to $10,598,575, with interest cumulative at the rate of five per cent per annum from July 10, 1933, and the maturity date for all of the bonds fixed as October 1, 1943; that under said Indenture your petitioner was not set up as a liquidating company but was authorized to do new business and permitted to acquire bonds and mortgages maturing five years later than its bonds, or October 1, 1948; that since the execution and delivery of said Indenture, your petitioner has operated and conducted its business and affairs in accordance with and subject to the provisions of said Indenture; that interest on said bonds at the rate of five per cent per annum, cumulative, has been payable solely out of earnings, and during that time, petitioner has paid approximately three per cent per annum interest to bondholders, and approximately two per cent interest per annum has accumulated; that your petitioner's financial condition and the character of its assets have been greatly improved despite the depression, mortgage moratorium laws and generally unfavorable conditions existing in the real estate field during the past ten years; that petitioner has acquired by purchase and now holds in its treasury its own bonds in the principal amount of $4,888,175, and its remaining bonds now outstanding are in unpaid principal amount of $5,710,400, with accumulated and unpaid interest thereon from July 10, 1933 to April 10, 1943, amounting to $1,167,679.76. These bonds mature October 1, 1943, at which time the accumulated unpaid interest becomes due and payable with the principal. There is not now and there has been no default on said bonds or under said Indenture. Petitioner has no other obligations except current bills.

4. Your petitioner is unable to pay its debts as they mature.

5. The assets, liabilities, capital stock and financial condition of your petitioner as of June 30, 1943 are as follows:

Petition.

BALANCE SHEET, JUNE 30, 1943

Assets

Cash in banks		$1,108,737.63
Legal investments at book value (quoted market value $1,760,069.00)		1,793,192.15
Miscellaneous investments at book value:		
Bonds and mortgage certificates	$ 879,853.29	
Capital stocks of affiliated corporations	6,050.00	
		885,903.29
Notes Receivable		22,453.67
Accounts receivable		23,964.12
Bonds and mortgages receivable—Principal outstanding		4,164,751.46
Installment contracts receivable—Principal outstanding	$ 300,976.19	
Less—Principal amount of mortgages on properties sold under installment contracts	88,417.59	
		212,558.60
Advances made for mortgagors and purchasers under installment contracts	1,483.06	
Less—Reserve for uncollectible accounts	857.58	
		625.48
Real estate, carried at book value	7,475,871.52	
Less—Principal amount of mortgage liens thereon	5,895,558.12	
		1,580,313.40

Other investments:		
Realty Associates Securities Corporation 5% stamped bonds due 1943 in the principal amount of $4,888,175.00, at cost	2,178,044.13	
Securities purchased with funds that were part of the $23,801.23 reserve, per contra, for losses on mortgages purchased guaranteed, at cost	19,944.59	
		2,197,988.72
Investments in capital stocks of wholly-owned corporations		166,330.11
Deferred charges and items held in suspense		6,900.20
Total Assets		$12,163,718.83
Deficit (based on book values and subject to note below):		
Operating deficit, beginning July 10, 1933	$1,624,864.20	
Less—Paid-in surplus	323,108.03	
		1,301,756.17
		$13,465,475.00

LIABILITIES

Accounts payable:		
Collections made by corporation as agent	$ 19,083.57	
Coupons payable on old bonds $1,758.00		
Less—Funds with paying agent 1,626.00		
	132.00	
Miscellaneous	2,868.18	
		$22,083.75

Interest payable on 5% stamped bonds due October 1, 1943, issued or to be issued (see note):		
Accumulated and accrued interest	2,414,528.55	
Less—Excess cash on deposit with Trustee	73.34	
	2,414,455.21	
Less—Cash on deposit with Trustee for interest distributable to bondholders July 1, 1943	158,978.63	
		2,255,476.58
Liability for 5% stamped bonds due October 1, 1943:		
Bonds issued (including $4,888,175.00 of bonds acquired by the corporation at a cost of $2,178,044.13—see contra)	10,551,400.00	
Bonds to be issued for old 6% bonds which have not yet been presented to the Trustee for reduction and modification	47,175.00	
		10,598,575.00
Principal amount of old 6% bonds uncancelled	162,525.00	
Less—Principal amount of bonds on hand with corporation and trustee, to be used, if necessary, as explained in the attached report (accountant's report)	162,525.00	
		* * *
Deferred credits and items held in suspense:		
Unearned discounts on mortgages and installment contracts	560,276.48	

Deposits on leases and sales	1,590.00	
Unrealized income, unapplied collections of mortgage principal, and other items held in suspense	2,171.96	
		564,038.44
Reserve for losses on certain mortgages purchased guaranteed ($19,944.59 of this reserve has been invested in securities—see contra)		23,801.23
Capital stock (authorized and issued): 300 shares of no par value—Declared value of $5.00 per share		1,500.00
		$13,465,475.00

NOTE: The accumulated and accrued interest payable aggregating $2,414,528.55 includes $1,113,606.12 which is applicable to the $4,888,175.00 of bonds owned by the corporation and held as investments at June 30, 1943. This interest receivable of $1,113,606.12 has not been set up in the books, as the bonds to which it relates are income bonds, and such interest, therefore, would not be received (or the liability cancelled) by the corporation until maturity (unless the bonds were cancelled), in which case the relative amount of accrued interest receivable on such cancelled bonds would offset a corresponding amount of the interest payable set up in the books. As the bonds are traded in at a flat price, if the corporation should sell any of them the subsequent owners would normally receive all of the interest, when, as, and if paid. No part of the above-mentioned interest receivable of $1,113,606.12 has been reflected in this or any of the statements contained in the report.

The foregoing balance sheet is the latest available and taken from the Report on Audit and Accounts for the three months ended June 30, 1943, made by Stagg, Mather & Hough, of 141 Broadway, New York City, who are independent public accountants selected in accordance with the

provisions of said Indenture, dated as of July 10, 1933, and approved by Manufacturers Trust Company, Trustee under said Indenture, and by the four representatives on the Board of Directors of your petitioner selected by the bondholders pursuant to said Indenture, and the said Report on Audit and Accounts, including said balance sheet, is on file with the said Trustee and is subject to the comments contained in said Report.

The said bonds shown on said balance sheet in principal amount $4,888,175, which the Corporation acquired by purchase, are held in the treasury of your petitioner ready and available for cancellation in conjunction with a plan of reorganization; and, upon such cancellation, the above stated deficit (based on book values) shown on said balance sheet in amount $1,301,756.17 will be changed into a surplus (based on book values) of $2,521,980.82 thereby more clearly showing the financial condition of your petitioner.

It is believed that, as at the date of the verification of this petition, the figures above set forth in the balance sheet remain substantially the same, except as the balance sheet changes to reflect the transaction of your petitioner's business and affairs in the ordinary course of business subsequent to the date thereof, and that the accrued interest on funded debt has increased by lapse of the intervening time, and the petitioner's cash on hand and in banks is at present approximately $1,261,000.00.

6. The nature of all pending proceedings affecting the property of the Corporation known to your petitioner, and the courts in which they are pending, are set out in detail in Exhibit "A" annexed hereto and made a part hereof. An examination of this exhibit reveals that these proceedings consist largely of mortgage foreclosure or certiorari proceedings.

7. No plan of reorganization, readjustment or liquidation affecting the property of your petitioner is pending in connection with any judicial proceeding. A voluntary Plan for Reduction and Extension of your petitioner's bonds was formulated and sent to all bondholders on July 30, 1943, as more completely set forth in the following paragraph.

8. The specific facts showing petitioner's need for relief under Chapter X of said Act are as follows: Your petitioner's assets are of a value in excess of its total liabilities

inclusive of its capital stock but the nature of its assets, being in large part real estate and real estate securities, is such that their true value is not readily realizable; a forced sale of said assets would bring substantially less than their true value and under existing war time conditions and by reason of the moratorium statutes of the State of New York, might bring even less than its total liabilities exclusive of its capital stock; your petitioner's financial condition and situation is such that insistence by its bondholders upon payment of their bonds in full at maturity, October 1, 1943, would lead to many actions and proceedings against it, recovery of judgments against it, levy of execution against its assets, interference with and destruction of its business and property, with resulting loss to creditors and destruction of rights of stockholders. The adoption of a suitable plan of reorganization under said Act will protect the bondholders and other creditors of your petitioner and will reduce the loss to its stockholders which would otherwise result from the enforcement of bondholders' claims and consequent destruction of your petitioner's business and sacrifice and loss in the value of its properties. It is essential for the protection of creditors and stockholders that the commencement of suits against your petitioner be stayed pending final decree in this proceeding.

Your petitioner prepared and on July 30, 1943 forwarded to all bondholders of record a "Plan for Reduction and Extension of the Bonds of Realty Associates Securities Corporation, maturing October 1, 1943", a copy of which is annexed hereto, made a part hereof and marked Exhibit "B".

In substance, said Plan provides for cancellation and retirement of all bonds owned by your petitioner, together with accumulated interest thereon, a payment of fifteen percent of the principal amount of each remaining outstanding bond upon the Plan becoming effective, a payment of twenty-five percent of the accumulated interest to bondholders upon the Plan becoming effective and payment of the balance in three annual installments, the extension of the maturity date of the bonds as so reduced to October 1, 1953, and modification of the interest rate and a change in the method of computing earnings from which the interest, a part of which was to be based on earnings, was to be paid. A proposed Supplemental Indenture, dated as of October 1, 1943, was prepared, embodying in detail the

changes contemplated by the said Plan in the aforesaid Indenture, dated as of July 10, 1933, and containing provisions for the protection of bondholders in accord with the Trust Indenture Act of 1939, and said Indenture and Supplemental Indenture were duly qualified with the Securities and Exchange Commission by its order dated July 21, 1943.

At the date of the verification of this petition, 1,450 bondholders holding in the aggregate $3,601,950, of the principal amount of bonds outstanding (excluding the bonds owned by your petitioner) have signified in writing their assent to said Plan. In addition, holders of a large amount of bonds have stated that they favor said Plan provided all bondholders receive the same treatment. It is therefore believed that a plan of reorganization can speedily be worked out under the supervision and protection of the Court, thereby preventing possible partial loss to petitioner's creditors and heavy loss to its stockholders.

The specific facts showing why adequate relief cannot be obtained under Chapter XI of said Act are as follows: Because of the large unpaid principal amount of bonds outstanding, $5,710,400 (which is exclusive of bonds owned by petitioner), and the large number of bondholders, approximately 2,300, your petitioner may not resort to the ordinary form of arrangement with its bondholders under Chapter XI of said Act and the Plan which has been prepared does not lend itself for treatment under said Chapter XI of said Act.

9. Your petitioner desires that a plan or reorganization be effected for it under and pursuant to Chapter X of said Act.

10. The indebtedness of your petitioner, liquidated as to amount and not contingent as to liability, is over $250,000, and a trustee is to be appointed under Chapter X of the Bankruptcy Act who shall be disinterested. Petitioner desires that, for the purposes specified in Section 189 of the Bankruptcy Act, an additional trustee be appointed, and desires that such additional trustee be Jerome Thralls, who has been a director of your petitioner for eight years and is thoroughly familiar with its business and affairs.

11. This petition is filed in good faith; and in view of the response of petitioner's bondholders in a period of only

two months to the aforesaid Plan for Reduction and Extension of its Bonds, referred to in more detail in paragraph "8" above, it is not unreasonable to expect that a plan of reorganization of the petitioner can be effected.

12. No other petition by or against your petitioner is pending under Chapter X of said Act, nor is any other bankruptcy proceeding initiated by a petition by or against your petitioner now pending.

13. The stock of your petitioner and the stock of Realty Associates, Inc., a corporation organized and existing under the laws of the State of New York, which is the owner of and engaged in the development, management and operation of real property, is owned by the same stockholder, Consolidated Realty Corporation, a corporation organized and existing under the laws of the State of New York, having its principal place of business at No. 33 Liberty Street, New York City. For many years, your petitioner and Realty Associates, Inc. have had and maintained and now do have and maintain joint offices at No. 162 Remsen Street, Brooklyn, New York, and their officers and employees have been and now are almost identical; and these companies, through their association, have each enjoyed substantial savings in overhead costs and substantial financial benefits. The directors of your petitioner, four of whom are designated by bondholders, and the directors of Realty Associates, Inc. have from time to time apportioned between the two companies the salaries and wages of their officers and employees in accord with their judgment as to the proper allocation thereof based upon the services rendered by the officers and employees to each of the companies. At present your petitioner is defraying 67½ percent of the salaries and wages of the officers and employees of the two companies and Realty Associates, Inc. is defraying 32½ percent of such salaries and wages. Your petitioner believes that proportion now is the fair and reasonable apportionment of such costs between the companies. In the interest of sound, efficient operation and administration of the business and assets of your petitioner, petitioner asks that such arrangement be continued until otherwise ordered by this Court. (For the year 1942, this apportionment was 70 percent to your petitioner and 30 percent to Realty Associates, Inc.)

Petition.

14. Petitioner desires that until the qualification of such trustee and additional trustee as may be appointed, or until further order of the Court, petitioner be authorized to continue the employment of its officers, as set forth in the affidavit filed herein pursuant to Bankruptcy Rule X-3 of this Court, at the rates of compensation therein set forth, and on the basis of apportionment outlined in paragraph "13" above and to continue to operate and maintain its property and business, to pay salaries, wages, carrying charges and other expenses of operation and maintenance of its property and business as they mature and, if applicable, on the basis of apportionment outlined in paragraph "13" above, to pay current accounts payable for wages and other expenses of operation and maintenance of its property and business, to continue performance of its existing contracts for the purchase or sale of bonds and mortgages and real estate, and its other contracts and agreements including the agreement for apportionment of salaries and wages outlined in paragraph "13" above, and to take any and all other action deemed necessary to continue the operation and maintenance of its property and business. The payroll for the officers and office employees, consisting of about 68 persons, and for the employees in buildings owned by petitioner, consisting of about 10 persons, and any other classes of employees, is paid weekly, semimonthly and monthly. Your petitioner believes that failure to meet such costs, expenses, charges and payroll promptly might seriously disrupt and injure petitioner's business.

15. The Board of Directors of the petitioner duly authorized and directed the filing of this petition by resolutions duly adopted at a meeting of said Board of Directors held September 28, 1943, a copy of which resolutions, certified by the Secretary of the petitioner, is annexed hereto, marked Exhibit "C", and made a part hereof.

WHEREFORE, your petitioner prays

(a) That an order be entered herein approving this petition as properly filed under said Chapter X;

(b) That Jerome Thralls be appointed an additional trustee for the purposes specified in Section 189 of the Bankruptcy Act;

(c) That the petitioner be authorized, until further order of the Court or until further action by any trustee appointed herein, to continue the employment of its officers as set forth in the affidavit filed herein pursuant to Bankruptcy Rule X-3 of this Court, at the rates of compensation in said affidavit set forth and on the basis of apportionment outlined in paragraph "13" herein;

(d) That the petitioner be authorized, until the qualification of a trustee appointed herein, to operate and maintain its property and business, to pay salaries, wages, carrying charges and other expenses of operation and maintenance of its property and business as they mature and, if applicable, on the basis of apportionment outlined in paragraph "13" herein, to pay current accounts payable for wages and other expenses of operation and maintenance of its property and business, to continue performance of its existing contracts for the purchase or sale of bonds and mortgages or real estate, and its other contracts and agreements including the agreement for apportionment of salaries and wages outlined in paragraph "13" herein, and to take any and all other action deemed necessary to continue the operation and maintenance of its property and business;

(e) That a plan of reorganization of the petitioner be effected pursuant to Chapter X of the Bankruptcy Act, and that your petitioner be granted all other and further relief to which it may be entitled.

REALTY ASSOCIATES SECURITIES CORPORATION
By: Harry D. Burchell
Vice-President of said Corporation
Petitioner.

Vincent Rowan
Treasurer of said Corporation,
Petitioner.

UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT

In the Matter

of

REALTY ASSOCIATES SECURITIES CORPORATION,

Debtor.

In the Matter of the Determination of the Amount of Interest Payable in Respect of the Debtor's Bonds After Maturity.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,

Appellants.

I, ALEXANDER M. BELL, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the attached was used on the argument of the above entitled case in this court.

ALEXANDER M. BELL
Clerk

by A. DANIEL FUSARO
Deputy Clerk

Dated: August 28, 1947

United States Circuit Court of Appeals
FOR THE SECOND CIRCUIT.

In the Matter

of

REALTY ASSOCIATES SECURITIES CORPORATION,
Debtor.

In the Matter of the Determination of the Amount of Interest Payable in Respect of the Debtor's Bonds after Maturity

MANUFACTURERS TRUST COMPANY,
Appellant.

EXHIBITS #4 AND #5 REFERRED TO AT PAGE 21 OF APPELLANT'S BRIEF.

HANDED UP AT THE ARGUMENT, PURSUANT TO STIPULATION (fol. 614).

Exhibit #4.

At Brooklyn, New York, in the said Eastern District of New York, on the 15th day of June, 1944.

This cause coming on further to be heard upon the order to show cause granted herein May 26, 1944, upon the petition of HUNTER L. DELATOUR and RAYMOND REISLER, Esqs., verified the 26th day of May, 1944 and the affidavit of JEROME THRALLS, Esq., sworn to the 26th day of May, 1944, for instructions regarding the making of a further payment to the bondholders of the outstanding bonds of the Debtor,

Now, upon reading the order to show cause granted herein May 26, 1944, together with the petition of HUNTER L. DELATOUR, Esq., and RAYMOND REISLER, Esq., verified the 26th day of May, 1944, and the affidavit of JEROME THRALLS, sworn to the 26th day of May, 1944, upon which said order to show cause was granted, and upon reading the notice of motion of LEWIS, MARKS & KANTER and JULIUS SILVER, attorneys for Bondholders' Protective Committee, dated June 7, 1944, and the affidavit of EDWARD B. MEREDITH, sworn to the 8th day of June, 1944; the notice of motion of ARCHIBALD PALMER, attorney for Anna A. Kuhlmann and Catherine Kuhlmann, bondholders, together with the petition of said Anna A. Kuhlmann and Catherine Kuhlmann, verified the 5th day of June, 1944; and the notice of motion of JOSEPH R. MARGULIES, attorney for bondholders, Ernestine Needles, et al., dated June 7, 1944, all submitted in connection herewith; and after hearing HALPIN and KEOGH, Esqs., attorneys for the Trustees herein (by Eugene J. Keogh, of counsel); ARCHIBALD PALMER, attorney for Anna A. Kuhlmann and Catherine Kuhlmann, bondholders; LEWIS, MARKS & KANTER and JULIUS SILVER, Esqs., attorneys for Bondholders' Protective Committee (Jack L. Rappaport, Esq., of counsel); GEORGE ZOLOTAR, Esq., attorney for Securities and Exchange Commission; JOSEPH R. MARGULIES, attor-

ney for Ernestine Needles, et al.; HERRICK and FEINSTEIN, Esqs., attorneys for Bondholders' Directors Committee (Abraham Feinstein, Esq., of counsel); CHARLES J. BUCHNER, Esq., attorney for M. C. O'Neill, bondholder; NEWMAN & BISCO, Esqs., attorneys for the Indenture Trustee and for the bondholders serving in the armed forces (Perry A. Hull, Esq., of counsel); ROOT, CLARK, BUCKNER and BALLANTINE, Esqs., attorneys for Consolidated Realty Corporation (William P. Palmer, Esq., of counsel); HOOKER, ALLEY and DUNCAN, Esqs., attorneys for the Debtor (James B. Alley, Esq., of counsel); PERCIVAL E. JACKSON, attorney for John Vanneck, et al., and the court having reserved decision with respect to the making of any payment on account of the unpaid principal of the outstanding bonds of the Debtor and no objection having been made to the payment by the Trustees herein of interest on said bonds

NOW, upon motion of HALPIN and KEOGH, attorneys for the Trustees herein, it is

ORDERED that said application be and the same hereby is granted to the extent that HUNTER L. DELATOUR and RAYMOND REISLER, as Trustees, and JEROME THRALLS, as additional Trustee, be and they hereby are authorized and permitted to make a payment of interest at the rate of 3% per annum on July 1, 1944, to all the holders of the outstanding stamped bonds of the Debtor, and it is further

ORDERED that the said Trustees and additional Trustee may employ a paying or disbursing agent for the purpose of preparing, drawing and mailing the checks in payment of the interest above provided and may pay such agent a sum not to exceed Three hundred seventy-five ($375) Dollars, for its fees for such services, plus its actual disbursements for printing, stationery and postage at cost.

GROVER M. MOSCOWITZ,
United States District Judge.

Exhibit #5.

HUNTER L. DELATOUR, Esq., and RAYMOND REISLER, Esq., as Trustees of Realty Associates Securities Corporation, Debtor, having moved this Court for an order authorizing and permitting the said Trustees to make a payment of interest for the period of six months from May 1, 1944 to October 31, 1944, at the rate of 3% per annum, on January 1, 1945, to all the holders of outstanding stamped bonds of the Debtor, and such motion having duly come on to be heard on December 15, 1944,

Now, on reading and filing the petition of Hunter L. Delatour, Esq., and Raymond Reisler, Esq., verified December 8, 1944, in support of said motion; the order to show cause dated December 8, 1944 with proof of due service thereof upon the attorneys for all interested parties who have appeared herein, and after hearing HALPIN & KEOGH, attorneys for the Trustees, by Edward S. St. John, Esq., of counsel, in support of said motion, and after hearing George Zolotar, Esq., attorney for Securities and Exchange Commission, in favor of payment of interest for such period at the rate of 5% per annum; Lewis, Marks & Kanter, and Julius Silver, Esq., attorneys for Bondholders' Protective Committee, by Lloyd B. Kanter, Esq., of counsel, in favor of payment of interest for such period at the rate of 5% or 6% per annum; and Joseph R. Margulies, Esq., attorney for Bondholders Ernestine Needles, et al., in support of the payment of interest for such period at the rate of 6% per annum; Hooker, Alley & Duncan, attorneys for the Debtor, by James B. Alley, Esq., of counsel, in support of payment of interest for such period at the rate of 3% per annum and in opposition to payment at a higher rate; and Percival E. Jackson, Esq., attorney for Bondholders John Vanneck, et al., by Theodore N. Tarlau, Esq., of counsel; Newman & Bisco, attorneys for Manufacturers Trust Company as Indenture Trustee and for persons in the Mili-

tary Service, by Perry A. Hull, Esq., of counsel; Root, Clark, Buckner & Ballantine, attorneys for Consolidated Realty Corporation, by William P. Palmer, Esq., and L. Robert Driver, Esq., of counsel; Arthur O. Asher, Esq., attorney for Max L. Bliss, et al., bondholders; Irving L. Schanzer, Esq., attorney for Prudence Realization Corporation; James A. Dealy, Esq., attorney for Amalgamated Properties, Inc.; Lynn G. Goodnough, Esq., attorney for Realty Associates, Inc.; Chester Allen, Esq., attorney for Kings County Trust Company, appearing but not opposing, and due deliberation having been had,

Now, on motion of Halpin & Keogh, attorneys for the Trustees, it is

Ordered that the said motion be and the same hereby is granted to the extent of authorizing and directing Hunter L. Delatour, Esq., and Raymond Reisler, Esq., as Trustees of Realty Associates Securities Corporation, Debtor, on January 1, 1945, to make a payment of interest at the rate of 5% per annum for the period from May 1, 1944 to October 31, 1944, to all the holders of outstanding stamped bonds of the Debtor, and it is further

Ordered that the said Trustees may employ a paying or disbursing agent for the purpose of preparing, drawing and mailing the checks in payment of the interest so provided, and may pay such agent a sum not to exceed the sum of $375 for its fees, for such services, plus its actual disbursements for printing, stationery and postage at cost.

Dated: Brooklyn, New York, December 21st, 1944.

G. M. MOSKOWITZ,
United States District Judge.

UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT

In the Matter

of

REALTY ASSOCIATES SECURITIES CORPORATION,

Debtor.

In the Matter of the Determination of the Amount of Interest Payable in Respect of the Debtor's Bonds after Maturity

---

MANUFACTURERS TRUST COMPANY,

Appellant.

I, ALEXANDER M. BELL, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the attached was used on the argument of the above entitled case in this Court.

ALEXANDER M. BELL
Clerk

by A. DANIEL FUSARO
Deputy Clerk

Dated: September 4, 1947.

(Seal)

FILE COPY

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FILED
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CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

October Term, 1947

In the Matter of

REALTY ASSOCIATES SECURITIES CORPORATION,
Debtor.

No. 405

MANUFACTURERS TRUST COMPANY, Indenture Trustee,
Petitioner,

v.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,
Respondents.

No. 406

EDWIN B. MEREDITH, JACOB R. SCHIFF and MILTON C. ZAIDENBERG, as Members of the Bondholders' Protective Committee,
Petitioners,

v.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,
Respondents.

No. 407

VANNECK REALTY CORPORATION,
Petitioner,

v.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,
Respondents.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION IN SUPPORT OF PETITIONS

Legal Intelligencer, 1218 Chestnut St., Phila. 7, Pa.

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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1947

In the Matter of

REALTY ASSOCIATES SECURITIES CORPORATION,
Debtor.

No. 405

MANUFACTURERS TRUST COMPANY,
Indenture Trustee, *Petitioner,*

v.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,
Respondents.

No. 406

EDWIN B. MEREDITH, JACOB R. SCHIFF and MILTON C. ZAIDENBERG, as Members of the Bondholders' Protective Committee, *Petitioners,*

v.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,
Respondents.

No. 407

VANNECK REALTY CORPORATION,
Petitioner,

v.

REALTY ASSOCIATES SECURITIES CORPORATION and CONSOLIDATED REALTY CORPORATION,
Respondents.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION IN SUPPORT OF PETITIONS

The respondent Consolidated Realty Corporation is a corporation all of whose stock is owned by the Reconstruction Finance Corporation. Consolidated Realty Corporation, in turn, owns all of the stock of the debtor, Realty Associates Securities Corporation. The Securities and Exchange Commission is a statutory party herein pursuant to Section 208 of the Bankruptcy Act, 11 U.S.C. § 608, and its position in the instant matter in support of the petitions for certiorari is contrary to that of the Reconstruction Finance Corporation. In view of the conflicting positions of these two governmental agencies, I am authorizing each to present a brief in its own name. *Cf. Consolidated Realty Corp.* v. *Meredith, et al.*, 323 U.S. 758 (1944).

PHILIP B. PERLMAN,
Solicitor General.

OPINIONS BELOW

The opinion of the District Court (R. 171) is reported at 66 F. Supp. 416. The opinion of the Circuit Court of Appeals (R. 209), modifying the order of the District Court, is reported at 163 F. 2d 387.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 23, 1947 (R. 222). The petitions for writs of certiorari were filed on October 20, 1947. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, 28 U.S.C. §347(a), and Section 24(c) of the Bankruptcy Act, as amended, 11 U.S.C. §47(c).

QUESTIONS PRESENTED

(1) Whether the substantive rights of creditors to accrue interest on their claims are less in a Chapter X reorganization than in straight bankruptcy?

(2) Whether creditors holding matured and undisputed claims against the debtor on the date of a voluntary Chapter X petition, which claims consist of unpaid principal and interest, and which were prevented from being reduced to judgment by the debtor's resort to Chapter X, are entitled as against a sole stockholder upon dismissal of the proceedings and the return of the properties to the solvent debtor (a) to interest on the entire amount of their claims, including that portion representing interest accrued prior to the filing of the petition, and (b) to accrue such interest as may be allowed at the rate applicable to judgments rather than the contract rate.

STATEMENT OF FACTS

The debtor, Realty Associates Securities Corporation, deals in mortgages and other real estate interests (R. 4-5) and the respondent, Consolidated Realty Corporation, is its sole stockholder (R. 7). The Chapter X petition was filed by the debtor on September 28, 1943 in contemplation of the imminent maturity of a large publicly held bond issue due three days later, October 1, 1943 (R. 6). This was the principal (and practically the sole) indebtedness of the debtor, and its petition alleged that while the value of its assets exceeded "total liabilities inclusive of its capital stock," a forced sale might bring in less than the true value of the assets to the detriment of the stockholder interests (R. 6).

The bonds were originally issued in three series of $5,000,000 each in 1925, 1927, and 1928, due 1937, 1939, and 1943, respectively (R. 5; 8), and bore unconditional rights to 6% interest semi-annually (R. 42; 52; 62). On July 10, 1933, when some $12,450,000 principal amount was still outstanding, the debtor filed a voluntary petition in bankruptcy (R. 5; 8). The bankruptcy proceeding was terminated the following year as the result of a composition effected by the debtor. The composition involved a 15% payment on account of the outstanding indebtedness, an

extension of the remaining debt (including all three bond issues) to October 1, 1943, and a reduction in the interest rate thereon from 6% unconditionally to 5% "if earned." (R. 78). An amended indenture, dated as of July 10, 1933, defined "earnings" for interest purposes to permit deductions of capital losses provided that such losses could not be used to reduce interest below 3% per annum (R. 78; 92). Unpaid portions of the 5% annual interest were made cumulative and payable out of future earnings, or unconditionally at maturity (R. 10; 92). As a result, instead of being wiped out by bankruptcy, the debtor obtained a ten year moratorium which included substantial alleviation of its interest obligation.

During the moratorium years which followed, the debtor paid approximately 3% per annum, and took advantage of the unique definition of earnings to defer the remainder, thus retaining for its own use money which otherwise would have been payable to the bondholders.[1] As the extended maturity date approached, the debtor found itself still owing $5,710,400 in unpaid principal (R. 6; 191) and $1,286,646.43 in unpaid interest (R. 5; 10; 191). According to the Chapter X petition, it then had assets with a book value of nearly $13,500,000 (App.[2] b4), including approximately $1,261,000 in cash. (App. b7) and $1,760,069 in readily marketable securities (App. b3). Despite the availability of liquid assets more than sufficient to satisfy all interest claims, no payment of these claims was proffered. Instead, the debtor first attempted, in July of 1943, to obtain another voluntary extension and composition of the indebtedness and, failing in this, resorted to Chapter X to stave off the enforcement remedies normally available to the bondholders.

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[1] See Statement of Earnings for the Six Months Ending April 30, 1943 (R. 138), for an illustration of the deduction of capital losses.

[2] "App." refers to the Appendices to Petitioners' Brief in No. 405, Filed Pursuant to Stipulation Dated September 26, 1947.

The Chapter X proceeding lasted nearly 18 months and was dismissed on April 2, 1945 on the petition of the debtor and its sole stockholder, Consolidated Realty Corporation (R. 7, 25). By that time the debtor's business situation and the value of its assets had improved sufficiently to persuade the stockholder respondent to advance it the funds necessary to discharge the indebtedness. The petition for dismissal, however, denied any liability for interest beyond 5% on the unpaid principal to April 15, 1945, the date fixed for payment and settlement (R. 26; 172). The court's dismissal order, provided for payment of the undisputed claims for principal and interest, and for a reserve to be retained by the Chapter X trustees sufficient to pay any additional amounts which might be allowed (R. 26 *et seq.*). Jurisdiction was reserved to adjudicate, *inter alia*, the dispute as to the proper interest rate and base, the specific issues with respect thereto being:

(1) Whether interest is payable after the institution of the Chapter X proceedings on that portion of the bondholders' claims which represented unpaid interest accrued prior to that date; and

(2) Whether interest on the bonds, matured as of October 1, 1943, accrued during the Chapter X proceedings at the rate of 5%, as the debtor and its sole stockholder contend is provided by the indenture, or at 6%, the judgment rate which the bondholders contend should equitably be applied since they were prevented from obtaining judgment by the debtor's petition for reorganization.

The District Court held that the bondholders were entitled to 6% judgment interest on their entire claim including unpaid principal and interest accrued to the date of maturity and the filing of the Chapter X petition [3] (R.

[3] Throughout these proceedings the date of the Chapter X petition and the maturity date of the bonds have been treated essentially as one; for, as previously noted, the petition was

171-181; 191). On appeal by the debtor and its sole stockholder, a majority of the Circuit Court of Appeals (Judges Swan and Learned Hand), construed the indenture as providing for a 5% rate of interest on the unpaid principal of the bonds after maturity,[4] and held that interest was payable at that rate and only upon the portion of the bondholders' claim which represented unpaid principal (R. 217). The judgment of the District Court was modified accordingly (R. 218). Judge Clark, dissenting, expressed the view that equitable considerations required the allowance of the 6% judgment rate of interest on the bondholders' entire claim, including interest accrued prior to the abortive Chapter X proceeding (R. 218).[5] The instant petitions for certiorari followed.

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filed only three days earlier and admittedly in contemplation of the imminent maturity of the bonds.

[4] While we believe that the indenture, properly construed, does not contain any applicable post-maturity rate of interest on the bonds and that, therefore, they bear the legal rate of interest after maturity, we do not press at this time our disagreement with the decision of the court below on this point. This interpretative issue is of no significance if petitioners are correct in contending that interest should be allowed on their claims as if they had been reduced to judgment.

[5] The Indenture Trustee had also appealed from another portion of the District Court's order which applied an interim payment first towards reduction of the bondholders' original claim, rather than upon the interest which had accrued during the course of the Chapter X proceedings (R. 191; 197). The Circuit Court found that such application produced a difference in the amount to which the bondholders were entitled only if more than 5% interest were payable, and in view of its holding as to the proper interest rate and base, regarded this aspect of the appeal as academic. Accordingly, this portion of the District Court's order was affirmed (R. 218).

ARGUMENT

The petitions present questions of importance in the administration of Chapter X of the Bankruptcy Act which we believe should be decided by this Court. The rights of creditors holding matured and undisputed claims against a debtor to accrue interest on those claims from the date of the petition at the rate applicable to judgments where, but for the petition, they would be entitled to reduce those claims to judgment and receive interest thereon at the judgment rate, is a federal question which, in the context of a reorganization proceeding, has not been, but should in our opinion be, considered by this Court. Improved business conditions and appreciations in asset realization values during the past few years have provided surpluses after payment of the principal of creditors' claims in many estates being administered under Chapter X, with resultant conflict between creditors and stockholders as to the validity and extent of the interest claims payable out of such surpluses. Thus, the question here presented is of recurrent importance under present business conditions.[6] We believe it was erroneously decided by the majority of the court below. In our opinion, the decision below introduces novel distinctions between allowable claims in straight bankruptcy and in Chapter X reorganizations which are unwarranted by the provisions and underlying purposes of the Bankruptcy Act. The determination below also runs counter to well established equitable doctrines applicable in federal liquidation and reorganization proceedings.

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[6] For example, aspects of this problem have recently been presented in the following reorganizations in which the Commission is a party: *In re Childs Company*, 69 F. Supp. 856 (S.D.N.Y. 1946), and S.E.C. Corp. Reorg. Release No. 67, C.C.H. Bankruptcy Law Service, par. 55,734; *In re United States Realty & Improvement Co.*, S.D.N.Y., Bkcy. No. 83280, order approving plan dated May 14, 1946, par. 18; *In re Equitable Office Bldg. Corp.*, S.D.N.Y. Bkcy. No. 78476, order approving plan dated October 24, 1947, appeals pending in the court below.

1. As previously noted, the decision below introduces a distinction between the allowable claims of creditors in straight bankruptcy and in Chapter X reorganization which is wholly unwarranted by the statute. The court below expressly recognizes that "allowed claims in bankruptcy are of the same efficacy as judgments with respect to bearing interest, where the assets of the bankrupt are sufficient" (R. 214). It had expressly so held in *In re John Osborn's Sons & Co.*, 177 Fed. 184 (1910),[7] a straight bankruptcy case, relying upon the ruling of this Court in *National Bank of the Commonwealth of New York* v. *Mechanics National Bank*, 94 U.S. 437 (1876). The latter case involved the liquidation of a New York bank under the National Banking Act [8] and the depositors were held to be entitled to interest on demand deposits from the date of demand at the rate applicable to judgments in the State of New York. This Court then stated (94 U.S., at 439):

> "If these claims had been put in judgment * * * the result as to interest upon the judgment would have been the same. It was unnecessary to reduce them to judgment, because they were proved to the satisfaction of the comptroller. After they were so proved, they were of the same efficacy as judgments, and occupied the same legal ground."

Insofar as the decision below treats the principal amount of the bonds as differing from the accrued interest as respects its status as an interest bearing claim, the decision is contrary to Section 63(a)(1) of the Act, 11 U.S.C.

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[7] Appellants in the court below attempted to distinguish the *Osborn* case because of the failure of the bankrupt in that case to make any contract for the payment of interest. The court below stated, however (R. 214): "Assuming without decision that the attempted distinction would be invalid in an ordinary bankruptcy, we are not convinced that the 'judgment theory' is applicable in a Chapter X reorganization. . . ."

[8] Recently, in *Vanston Bondholders' Protective Committee* v. *Green et al.*, 329 U.S. 156 at 165 (1946), in dealing with a specialized interest problem in a Chapter X proceeding, this Court referred to bank liquidation cases as involving analogous principles.

§ 103(a) (1), which is applicable to a Chapter X proceeding as well as an ordinary bankruptcy, and which provides that an allowable claim shall include a fixed liability of the debtor, together with any interest thereon which would have been recoverable at the date of the petition. Under this provision principal and interest accrued to the date of the petition are treated as part of the creditor's single claim against the estate, just as they would be treated as a single claim if reduced to judgment. Thus, in *Johnson* v. *Norris*, 190 Fed. 459 (1911), the Fifth Circuit Court of Appeals ruled that interest was payable on claims which, as filed, included interest accrued prior to the date of the bankruptcy petition, before any part of a surplus held by the trustee could be turned over to the bankrupt.[9] In the present case, at the date of the Chapter X petition the bondholders' claim against the debtor amounted to $6,997,046.43, of which $1,286,646.43 represented interest accrued and accumulated prior to the Chapter X proceedings. Contrary to the statute, the holding below denies the creditor the full right to treat the accrued interest as part of his claim for the purpose of an allowance of interest.

The majority of the Circuit Court of Appeals differentiated straight bankruptcy from reorganization, and decided that, in the latter proceeding, creditors possessing matured and undisputed claims which would have been reduced to judgment but for the Chapter X petition, were not entitled to have their claims for principal and accrued interest treated as if reduced to judgment because, in the majority's view, Chapter X contemplates a "moratorium" for the debtor precluding the recognition of those claims as "peremptory demands, like judgments, upon which dam-

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[9] In *Ohio Savings Bank & Trust Co.* v. *Willys Corp.*, 8 F. 2d 463 (1925), the court below, in an equity receivership proceeding, applied the same theory in allowing interest on creditors' claims, part of which had represented interest accrued prior to the institution of the proceedings.

ages in the form of interest for delay in payment" is payable (R. 214).[10]

The attempted differentiation is apparently predicated upon the assumption, a fallacious one as we show below, that the greater remedial restrictions imposed by Chapter X in the interest of facilitating reorganization, require a holding that the claims of creditors in Chapter X are less than in straight bankruptcy. On the contrary, Section 200 (11 U.S.C. §600) provides that the rights of creditors with respect to the property of the debtor shall be the same in Chapter X as in straight bankruptcy unless "inconsistent with the provisions of this chapter"; and there are no provisions which would indicate that the substantive claims of creditors are less in Chapter X than in straight bankruptcy. If anything, they may be greater: See *e.g.*, the broad definition of "claims" in Chapter X which is set forth in Section 106(1), 11 U.S.C. §506(1).[11] So far as we know, this purported distinction, which conflicts with basic provisions of the Bankruptcy Act and runs counter to its underlying policy, is made for the first time by the court below.

2. Apart from the express statutory mandate that the substantive rights of creditors in Chapter X shall conform

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[10] The decision below does not push the concept of moratorium to the point of disallowing as between creditors and the debtor any "damages in the form of interest," a result recognized to be contrary to settled authority. Instead, that portion of the claim which represents accrued interest, assumed to be a non-interest bearing claim under local law unless reduced to judgment, was continued as a non-interest bearing claim and the bondholders were allowed 5% interest on the unpaid principal, which the court below held to be the post-maturity interest rate provided by the indenture. See pages 12-17, *infra*, where we discuss the inequity of the concept of moratorium so applied.

[11] Section 106(1) provides that claims recognizable in Chapter X include "all claims of whatever character against a debtor or its property, except stock, whether or not such claims are provable under Section 63 of the Act and whether secured or unsecured, liquidated or unliquidated, fixed or contingent."

to those in ordinary bankruptcy, there are other important reasons why the substantive scope of a creditor's claim should not depend on whether Chapter X or straight bankruptcy is invoked. Thus, we believe that the choice of proceedings should depend upon the prospects of realizing or preserving through reorganization, values for the totality of interests affected which might be lost in a straight bankruptcy proceeding. However, if the amount of the creditor's claim which will be recognized is less in a Chapter X proceeding than in ordinary bankruptcy, basically irrelevant considerations will be introduced which will tend to intensify conflicts of interest between different classes of security holders as respects the appropriate choice of proceeding. In a case, such as the instant one, involving a controversy between a single class of creditors and the stockholder interests, the decision below can only have the effect of stimulating creditor opposition to the reorganization process.

The decision below also creates certain other difficulties in the administration of the Bankruptcy Act. For example, Section 238(1), 11 U.S.C. § 638(1), provides that where a Chapter X proceeding is ultimately converted into a straight bankruptcy liquidation, the proceeding shall be conducted so far as possible in the same manner and with like effect as if an involuntary petition in bankruptcy had been filed at the date of the Chapter X petition and a decree of adjudication entered when the Chapter X petition was approved. It would seem to follow from the doctrine enunciated by the majority of the court below that although judgment interest would be denied during the Chapter X "moratorium", it would be required to be allowed retroactively to the date of the original reorganization petition in the event that the proceedings were transferred to straight bankruptcy. It hardly needs to be emphasized that a creditor's substantive rights should not be based upon such a contingency.

Again, the determination below would afford an inequitable advantage to certain creditors in a case where,

because of special circumstances unrelated to the propriety of preferential treatment of their claims, these creditors were permitted by the Chapter X court to pursue their claims to judgments after the filing of the petition.[12] In the event that there are assets available for the payment of interest on allowed claims, the ruling below would require that interest be payable on the newly acquired judgments at the judgment rate while other creditors are relegated to the contract rate, which may be considerably lower. A similar situation would be presented had the instant petition been filed after the maturity date of the bonds (instead of before) and had some of the bondholders succeeded in obtaining judgments on their claims prior to the petition. The inequality which would result were the "moratorium" concept of the court below applied in these situations obviously conflicts with the underlying statutory policy of equality of distribution.[13]

3. In developing its concept of a "moratorium" purpose of Chapter X the court below misconceived the purpose of the restraints which Chapter X imposes upon the entry of judgments and introduced an arbitrary rule in conflict with the flexible equitable considerations governing the allowance of interest claims which this Court so clearly enun-

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[12] The fact that a stay of lawsuits against the debtor rests in the discretion of the reorganization court and is not mandatory under the statute [see Sections 57d, 113, 116(4), 11 U.S.C. §§ 93a, 513, 516(4)] negates the "moratorium" concept of the court below as a statutory prohibition against judgments and their incidents after institution of reorganization proceedings, including the accrual of interest on claims as if they had been reduced to judgment.

[13] Section 63(a)(5) of the Act, 11 U.S.C. § 103(a)(5), for example, endeavors to preserve the statutory policy of equality of distribution among creditors by providing that where claims are permitted to be reduced to judgment after the filing of a petition, costs and interest accrued between the date of the petition and the entry of judgment shall not be allowed as part of the creditor's allowable claim; but this does not destroy its status as a judgment.

ciated in *Vanston Bondholders Protective Committee* v. *Green*, 329 U.S. 156 (1946).

The purpose of the customary stay of action which the reorganization court has discretion to grant is to avoid a race of the diligent to obtain preferential access to the assets, to insure equality of treatment among creditors, to prevent piecemeal executions, and to provide an orderly and equitable liquidation or reorganization. The normal procedural remedies are thus rendered unavailable, but the purpose of this restraint does not include denial of the substantive rights to which creditors would have been entitled absent the statutory proceedings. As the court below recognizes, at least as regards a straight bankruptcy proceeding, those substantive rights include judgment rights to interest where the entry of judgment has been precluded by the institution of proceedings under the Bankruptcy Act. The greater restrictions imposed by Chapter X upon the exercise of normal creditor remedies, we believe, do not warrant diminution of the allowable claims of creditors in a reorganization under that Chapter. On the contrary, those added restrictions and the slower process of realizing upon a claim in Chapter X make it all the more imperative that the substantive rights of creditors be fully protected in the reorganization process.

The reasoning of the majority below that Chapter X contemplates a "moratorium" which precludes alteration of the contractual relationship between the debtor and its creditors prior to the effective date of a plan overlooks the fact that the contract dealt with would be incomprehensible unless negotiated with reference to the creditor's expectations of obtaining judgment rights. The contract itself provided for a 10-year moratorium of limited scope, including a reduction in the contract rate of interest from 6% to 5% together with contingent provisions for deferring the interest claim to maturity. Regardless of the dispute as to whether the modified contract should be construed as continuing interest at 5% after maturity in the absence of

action by bondholders to enforce their claims, it is inconceivable that bondholders would have consented to the composition had they understood that the debtor could by institution of reorganization proceedings obtain a further moratorium in which the accumulated arrears of interest would be treated as a non-interest bearing claim and the return on principal would continue reduced below the judgment rate.

In denying interest on that part of the bondholders' claim which represented prior unpaid interest, the majority below relied largely upon a local New York policy against the compounding of interest, a policy which it conceded would be inapplicable if the claims were treated as if merged into judgment (R. 217).[14] The court below, however, refused to treat the indebtedness at the date of the petition as a single interest bearing claim. In our view, the holding below is contrary to the provisions of Section 63(a)(1) of the Bankruptcy Act, discussed *supra*, pp. 8-9, and, in addition, contravenes the equitable considerations which this Court, in the *Vanston* case, *supra*, held applicable as respects the allowance of interest in a Chapter X reorganization to the exclusion of any rules under state law.

In the *Vanston* case, which involved a Chapter X reorganization, this Court pointed out that "the touchstone of each decision on an allowance of interest in bankruptcy and receivership has been a balance of equities between creditor and creditor, or between the creditors and the debtor" (329 U.S., at 165). "Where an estate (is) ample to pay all creditors and pay interest even after the petition was filed," this Court observed, "equitable considerations (are) invoked to permit payment of this interest to * * * creditor(s) rather than to the debtor" (329 U.S., at 164). While the actual holding in the *Vanston* case was to deny interest on interest coupons which had matured after the institution of reorganization proceedings, and which were

[14] See also the New York cases cited *infra* n. 16, which treat allowed claims in local insolvency proceedings as if merged into judgments.

left unpaid in consequence of restraints imposed in the course of judicial administration, this interest denial was based solely upon a merging of the equities as between the classes of security holders affected. The estate was insolvent and the proceedings had extended over a period of sixteen years—from equity receivership, to Section 77B, and eventually into Chapter X. The accruals of interest on the overdue coupons were so large that they ate deeply into assets which otherwise would have been available to the junior creditors. To have allowed this additional interest on interest would have enriched the first mortgage bondholders at the expense of the junior creditors whose equity in the estate would have been seriously diminished by the protraction of the proceedings. In effect, allowance of the interest sought by the first mortgage bondholders would have placed upon the junior creditors the expense of a reorganization instituted for the benefit of all creditors.

A similar equitable approach was taken by the court below in the railroad reorganization case of *In re New York, New Haven & Hartford R.R.*, 147 F. 2d 40 (1945), *cert. denied*, 325 U.S. 884 (1945), in which a secured creditor had been enjoined from realizing on pledged collateral at a time when it had substantial market value. By the time the reorganization plan was approved the collateral had become worthless. Under these circumstances the court below held (147 F. 2d, at 48) :

> "*The damage to the banks resulting from it (the injunction) ought not equitably to be saddled on them but on the parties for whose supposed benefit the restraint was imposed, and particularly is this true where the decline in the value of the collateral resulted from an act of the debtor itself.* In our opinion fair and equitable treatment requires that the damage caused the banks should be made good to them and that they should be classified as secured creditors to the extent to which they could have realized on their collateral had they not been restrained from selling . . ." (Italics supplied.)

Analogous principles have been applied in other federal liquidations and reorganizations,[15] and, although not controlling in these proceedings, the New York courts give effect to the same equitable considerations in insolvency proceedings.[16]

The instant controversy presents the converse of the *Vanston* case and involves considerations resembling those present in the *New York, New Haven & Hartford R.R.* case. We believe that the equitable doctrines there enunciated require denial of the windfall which the debtor's sole stockholder would reap if the bondholders' matured and undisputed claims were not treated as if merged into judgment. As the reorganization petition substantially admits, the proceedings were instituted for the purpose of safeguarding the stockholder's equity in the debtor's assets, and were dismissed only after the debtor's financial condition had improved sufficiently to warrant that stockholder in advancing funds to discharge the debt. In depriving the bondholders of all rights to interest on a substantial part of their claim which was reducible to judgment at the date of the petition, and in denying them the judgment rate of interest on the balance, a rate to which they would have

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[15] Thus, in *Bindseil* v. *Liberty Trust Co.*, 248 Fed. 112 (1917) in holding that rents and profits belonged ultimately to a mortgagee who was restrained by the bankruptcy court from collecting them pending bankruptcy, the Third Circuit Court of Appeals observed (248 Fed., at 115): "As we are dealing in this case with the equitable administration of bankrupt assets, where creditors' *legal rights are preserved but where their legal remedies are lost and equitable remedies are substituted, equity requires the new remedies to be as effective as the old in protecting and enforcing such rights.*" (Italics supplied.)

See also, *Associated Co.* v. *Greenhut*, 66 F. 2d 428 (C.C.A. 3, 1933), *cert. denied*, 290 U.S. 696 (1933); *In re Wakey*, 50 F. 2d 869 (C.C.A. 7, 1931); *Mortgage Loan Co.* v. *Livingston*, 45 F. 2d 28 (C.C.A. 8, 1930); *In re Torchia*, 188 Fed. 207, 208-209 (C.C.A. 3, 1911).

[16] See *e.g.*, *Dorland* v. *Fidelity Development Co.*, 104 Misc. 97, 99, 171 N.Y. Supp. 1000, 1001 (N.Y. Sup. Ct. 1918); *Skilton* v. *Cordington*, 185 N.Y. 80, 87, 77 N.E. 790, 792 (1906); *Hunting v. Blun*, 143 N.Y. 511, 38 N.E. 716 (1894); *Lang v. Lutz*, 180 N.Y. 254, 260, 73 N.E. 24, 26 (1905).

been entitled absent the abortive Chapter X proceeding, the holding below saddles the creditors with the burden of a reorganization instituted for the benefit of the debtor and its sole stockholder.

We note, in passing, the reliance placed by the majority below upon a number of cases in which the Interstate Commerce Commission and federal courts have approved plans of reorganization which contained provisions for the accrual of interest at the contract rate subsequent to the date of the reorganization petition. As the majority below concedes (R. 214-5), it does not appear that the question as to the proper rate of interest was ever raised or considered in those cases. The opinions and available financial manuals indicate that with one exception [17] those cases all involved claims whose normal maturity dates did not arrive until well after the petition for reorganization,[18] so that the equitable considerations for treating them as if reduced to judgment would appear to be lacking.[19] These cases, moreover, did not deny creditors the right to interest on a claim which was reducible to judgment at the date of the institution of Chapter X proceedings. In view of these circumstances, we do not believe that they are of any value as precedents in the instant controversy.

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[17] *In re Adolf Gobel, Inc.*, Bankruptcy No. 79,526, S.D. N.Y., plan approved June 1, 1944.

[18] Such were the facts in *Ecker* v. *Western Pacific R.R. Corp.*, 318 U.S. 448 (1943); *Brooks* v. *St. Louis-San Francisco Ry.*, 153 F. 2d 312 (C.C.A. 8, 1946), *cert. denied*, 328 U.S. 868 (1946); *Chicago, Rock Island & Pacific Railway Reorganization*, 254 I.C.C. 707 (1943); *In re McKesson & Robbins, Inc.*, 8 S.E.C. 853 (1941), cited by the court below.

[19] We do not urge that a claim which would normally mature after the Chapter X petition is entitled to judgment interest from the date of the petition. In our view, the contract interest governs to the date of normal maturity and, in the case of an undisputed claim, judgment interest thereafter. We do not argue for the allowance of judgment interest as of the date of an accelerated maturity caused by the institution of receivership or reorganization proceedings, since this acceleration may be regarded as a penalty which, under the *Vanston* case, should not be permitted to flow from the institution of such proceedings.